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Nos. 86-1380, 86-1424, and 87-469

In the Supreme Court of the United States

OCTOBER TERM, 1987

ARKANSAS PUBLIC SERVICE COMMISSION, ET AL.,
PETITIONERS

v.

FEDERAL ENERGY REGULATORY COMMISSION, ET AL.

ARKANSAS POWER AND LIGHT COMPANY, PETITIONER

v.

FEDERAL ENERGY REGULATORY COMMISSION, ET AL.

REYNOLDS METALS COMPANY, ET AL., PETITIONERS

v.

FEDERAL ENERGY REGULATORY COMMISSION, ET AL.

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*ON PETITIONS FOR A WRIT OF CERTIORARI TO
THE UNITED STATES COURT OF APPEALS FOR
THE DISTRICT OF COLUMBIA CIRCUIT*

**BRIEF FOR THE FEDERAL ENERGY REGULATORY
COMMISSION IN OPPOSITION**

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QUESTION PRESENTED

Whether the Federal Energy Regulatory Commission had jurisdiction under Part II of the Federal Power Act, 16 U.S.C. (& Supp. IV) 824 *et seq.*, to reallocate the capacity of an electric power generating facility among four wholly-owned subsidiaries of an integrated public utility holding company, where the four subsidiaries operate as an interstate power pool and the system decided to build the facility to serve its overall needs.

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-96a) is reported at 808 F.2d 1525.[1] A subsequent order on re-

[1] "Pet. App." refers to the appendix to the petition for a writ of certiorari in No. 86-1380.

hearing remanding the case for reconsideration of two issues not involved here is reported at 822 F.2d 1104. The orders of the Federal Energy Regulatory Commission (Pet. App. 141a-222a, 97a-140a) are reported at 32 F.E.R.C. ¶ 61,425 and 31 F.E.R.C. ¶ 61,305.

JURISDICTION

The judgment of the court of appeals was entered on January 6, 1987. On April 3, 1987, the court of appeals granted rehearing en banc (86-1380 Supp. Br. App. SA-1 to SA-2). On June 24, 1987, the court vacated its grant of rehearing en banc (86-1380 Supp. Br. App. SA-3 to SA-4). On the same day, the panel granted rehearing and vacated a portion of its opinion and judgment of January 6, 1987 (86-1380 Supp. Br. App. SA-5 to SA-6). The petitions in Nos. 86-1380, 86-1424, and 87-469 were filed on February 20, 1987, March 4, 1987, and September 22, 1987, respectively. On September 3, 1987, the court of appeals denied a further petition for rehearing and rehearing en banc filed by certain petitioners (86-1380 Supp. Br. App. SA-7 to SA-10). The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. Petitioner Arkansas Power & Light Co. (AP&L), and respondents Louisiana Power & Light Co. (LP&L), Mississippi Power & Light Co. (MP&L), and New Orleans Public Service, Inc. (NOPSI) are all wholly-owned subsidiaries of Middle South Utilities, Inc. (MSU), a public utility holding company established in 1949 under Title I of the Public Utility Holding Company Act of 1935, 15 U.S.C. 79 *et seq*. The four subsidiaries operate as a highly integrated electric power pool (Pet. App. 33a, 37a, 44a). They sell and exchange electricity at wholesale across state lines, to each other as well as to outside companies, and

they also sell electricity at retail in separate service areas in five states. All electricity on the Middle South system is centrally dispatched from the system's dispatch center at Pine Bluff, Arkansas. *Id.* at 288a-292a, 378a.

A systemwide Operating Committee has historically coordinated the planning of new generating capacity for the system and has attempted to equalize the costs of additional capacity among the four operating companies (Pet. App. 10a-13a).[2] Until the late 1960s, the MSU system added new generating units in the southern part of the system to take advantage of cheap oil and gas reserves in that area (*id.* at 13a). The system has since sought to meet projected increases in demand and to diversify its fuel base by adding coal and nuclear generating units (*ibid.*). The Operating Committee has made the major decisions concerning timing, location, and size of additional capacity, based on its assessment of systemwide needs and objectives (*id.* at 181a-182a). In an effort to equalize costs and promote economies of scale, the Operating Committee has, in effect, rotated the responsibility for financing, building, and operating these new generation units among the four operating companies (*id.* at 183a-189a, 190a-191a; see also *id.* at 13a-19a). The Operating Committee has, to that end, "assigned" to each operating company at least one nuclear unit (*id.* at 190a-191a).[3] The

[2] The system Operating Committee has five members, consisting of one representative from the holding company and one from each operating company (Pet. App. 10a).

[3] Various parties in the administrative proceedings disputed the contention that the Operating Committee "assigned" new generation units to operating companies and claimed that the companies had instead "volunteered" to finance and construct the units (Pet. App. 181a-182a). FERC ultimately determined that "[w]hether units were 'volunteered' for or 'assigned' is not so relevant as the fact that operating companies ended up with responsibility for the units only where all the system companies, jointly acting as the System Operating Committee, concurred that this was in the best interests of the system as a whole" (*id.* at 182a).

Committee assigned to AP&L the responsibility for financing and construction of the first two nuclear units, ANO 1 and 2, which were built in the early 1970s, and thereafter assigned nuclear units to the other three operating companies (*id.* at 13a-14a, 184a-187a, 394a-397a).

In July 1971, the Operating Committee decided that Grand Gulf would be built and that Units Nos. 1 and 2 would come on line in 1979 and 1980, respectively. Under the original plan, MP&L was assigned responsibility for financing and constructing Grand Gulf Unit No. 1 (Grand Gulf 1), and NOPSI was assigned responsibility for financing and constructing Grand Gulf Unit No. 2 (Grand Gulf 2). Responsibility for construction of both units, however, soon shifted to MP&L because of siting problems within NOPSI's jurisdiction. When it subsequently became apparent that MP&L could not finance the construction, MSU made a system decision in 1974 to form a generation subsidiary, Middle South Energy (MSE) (now Systems Energy Resources, Inc.), to be the vehicle for financing the project. MSE acquired from MP&L all of its right, title, and interest in the Grand Gulf project. Pet. App. 16a-17a, 294a-296a, 396a-398a.

By the late 1970s, it became evident that Grand Gulf's capacity would not be needed immediately to meet demand, which was lower than predicted in earlier forecasts (Pet. App. 396a-397a). MSU continued to build Grand Gulf 1 and 2 on the assumption that, because of the relatively low cost of nuclear fuel, the overall cost (fixed plus variable) per kilowatt hour would be less than that of alternative energy sources and that, upon completion, MSE would sell the plants' capacity at wholesale to each of the four operating companies, in amounts to be determined later (*id.* at 398a-400a). All four operating com-

panies provided credit support to enable MSE to receive financing, and each remains liable for an agreed percentage of Grand Gulf costs (*id.* at 397a-398a).

The investment cost of Grand Gulf 1 and 2 continued to increase dramatically because of regulatory delay, additional construction requirements, inflation, and increased financing costs. As a result, although the investment cost of the two Grand Gulf units combined had been projected to be $1.2 billion, the investment cost of Grand Gulf 1 alone was approximately $3 billion upon its completion; construction of Grand Gulf 2 was suspended. The investment and other fixed costs associated with Grand Gulf 1 are substantially higher per kilowatt than the costs of other power generated by the MSU system (with the exception of one other nuclear plant). Although fuel costs are lower for Grand Gulf 1 than for most nonnuclear system power sources, the overall cost per kilowatt hour is higher for Grand Gulf 1 than for other system sources because of its much higher investment costs. Because AP&L completed construction of both of its nuclear units, ANO 1 and 2, by 1980, its overall cost per kilowatt hour for these plants is much lower. Pet. App. 14a-15a, 146a n.2, 233a, 396a-401a.

Transactions among the operating companies in the Middle South system, including the sale and exchange of capacity and energy, have been governed by a series of "System Agreements" filed with FERC. These agreements have provided the contractual basis for planning and operating the companies' generating units on a single-system basis; they have also provided mechanisms for equalizing cost imbalances among the four companies that result from the system's method of planning and operating the units. Pet. App. 151a. In 1982, Middle South Companies filed with FERC the 1982 System Agreement, which set forth the terms and conditions for transactions among the four operating companies (except the sale of

power from Grand Gulf), and a Unit Power Sales Agreement (UPSA), which established wholesale rates for MSE's sale of capacity in Grand Gulf 1 (with an entitlement to the associated power) to the operating companies (*id.* at 19a). The 1982 System Agreement, like prior versions, established a scheme of "capacity equalization payments" designed to ensure that each company contributes proportionately to the total cost of generating power on the System.[4] The UPSA obliged the four operating companies to purchase the following specified percentages of Grand Gulf capacity: LP&L, 38.57%; MP&L, 31.63%; NOPSI, 29.80%; and AP&L, 0% (*id.* at 147a).[5]

2. Under Part II of the Federal Power Act, 16 U.S.C. (& Supp. IV) 824 *et seq.*, the Commission is responsible for ensuring that all rates or charges, made, demanded, or received by any public utility for or in connection with the transmission or sale of electric energy in interstate commerce, as well as all rules, regulations, practices, and contracts affecting those rates or charges, are just and reasonable (see 16 U.S.C. 824d(a)). FERC assigned the 1982 System Agreement and the UPSA to two different

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[4] These payments are intended to compensate for the imbalances created by the system's rotational scheme of adding capacity: the last company to add capacity would, because the plant is sized for system needs, typically have contributed more than its share of costs. While the method of computing the amounts of these payments has been different in different System Agreements, the overall result has been that each company contributes to the total costs of generating power on the system roughly in proportion to its share of the overall demand for electricity of the system. Pet. App. 10a-16a, 151a-153a, 357a-358a, 391a-392a.

[5] The allocation of Grand Gulf 1 distributes among the four companies the "capacity" of the plant (that is, the capacity to produce a certain amount of electricity), the entitlements to whatever energy is produced from that capacity, and the costs of both the capacity (the up-front "investment" costs of constructing the plant and other fixed costs) and the energy (including fuel and other variable costs).

administrative law judges for review. After administrative hearings, the judges concluded that the agreements, as filed, were not just and reasonable, and were unduly discriminatory because they allowed AP&L to avoid any financial responsibility for the costs associated with Grand Gulf 1 (Pet. App. 367a, 414a).

FERC reviewed these initial decisions, rendered in February 1984 (Pet. App. 374a-526a) and February 1985 (*id.* at 223a-373a), and issued its decision in June 1985. FERC agreed that the 1982 System Agreement and the UPSA, because they did not allocate a share of Grand Gulf 1 to AP&L, would not result in just and reasonable allocations of costs between the operating companies and "that some form of equalization of nuclear plant costs is necessary to achieve just[,] reasonable, and non-discriminatory rates among the MSU operating companies" (Pet. App. 191a (footnote omitted)). FERC determined that the "most equitable allocation" would be for the operating companies to share in the system's total investment in nuclear capacity (four units, including Grand Gulf 1) "roughly in proportion to each company's share of System demand" (*id.* at 192a). On that basis, FERC ordered the following allocation of Grand Gulf 1 capacity and costs: AP&L, 36%; LP&L, 14%, MP&L, 33%; and NOPSI, 17% (*ibid.*).

In reaching its decision, FERC made two factual findings important to the present issue. First, FERC found that neither Grand Gulf 1, nor any one operating company, could be viewed in isolation: "the Middle South companies constitute a highly coordinated integrated electric system," which historically has "roughly equalized" generating costs among the four operating companies (Pet. App. 172a, 190a); the system Operating Committee made all "major critical decisions, including decisions to build new generating units, * * * for the benefit of the

system as a whole" (*id.* at 173a);[6] FERC specifically found that Grand Gulf 1 was no exception and had been planned to meet system needs (*id.* at 183a, 189a-191a). Second, FERC found that Grand Gulf 1 was part of a reasonable system plan to diversify the system's fuel base by developing nuclear power to meet anticipated demand (*ibid.*).

FERC rejected contentions advanced by several parties, including petitioners, that FERC lacked jurisdiction to reallocate the costs of Grand Gulf 1 among the four operating companies (Pet. App. 167a-170a). The Commission agreed with the two administrative law judges (*id.* at 306a-313a, 427a-439a) that neither the Federal Power Act provision denying FERC jurisdiction over generating facilities (Section 201(b)(1), 16 U.S.C. 824(b)(1)), nor any limitation on FERC's authority to compel a purchase or sale of power, precludes FERC's jurisdiction to reallocate the costs of Grand Gulf 1. The Commission noted "that the issue here is not whether a company should be forced to purchase or sell power, but rather is the appropriate allocation of costs among integrated companies owned by the same parent" (Pet. App. 169a). With respect to AP&L, in particular, the Commission "reject[ed] any assertion * * * that AP&L has had no involvement in the Grand Gulf unit * * *. AP&L has been continuously involved in the system decisions regarding Grand Gulf and MSE" (*id.* at 169a-170a). Finally, FERC likewise rejected (*id.* at 171a-172a) claims that its allocation order unduly impinged on state authority and was inconsistent with the Public Utility Holding Company Act of 1935, 15 U.S.C. 79 *et seq.*

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[6] The individual operating company responsible for a particular unit decided only subsidiary matters, such as the precise size or location of the unit, within the general guidelines set out by the system Operating Committee (Pet. App. 181a-182a; see also *id.* at 118a).

In subsequently denying several requests for rehearing, FERC further elaborated on the statutory basis for its authority to reallocate the capacity of Grand Gulf 1 among the four operating companies (Pet. App. 99a-113a). The Commission reiterated that it has "jurisdiction under Section 201 over the 1982 System Agreement because the agreement involves sales of electric energy at wholesale in interstate commerce" (Pet. App. 105a). The Commission also noted that the contrary view "would permit companies engaging in wholesale sales in interstate commerce to avoid the intended Federal regulation in Section 201(a) by forming a generation-only subsidiary to engage in the wholesale sales which otherwise would come under our jurisdiction" (Pet. App. 106a). Finally, the Commission stressed that, contrary to the premise underlying these jurisdictional challenges, AP&L is a "component part[]" of a highly integrated holding company system, whose interests must be "subsumed by the greater interests of the entire System" (*id.* at 129a).

3. On petition for review of FERC's orders, the court of appeals affirmed FERC's determination that it had jurisdiction to reallocate the capacity of Grand Gulf 1 among the four operating companies upon a finding that the two agreements as filed were unduly discriminatory (Pet. App. 1a-93a). On rehearing, however, the court vacated FERC's specific reallocation, remanding to FERC for a fuller explanation.[7]

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[7] On April 3, 1987, the panel had initially denied rehearing and the court of appeals had granted rehearing en banc to consider the terms of FERC's allocation (814 F.2d 773; 86-1380 Supp. Br. App. SA-1 to SA-2). On June 24, 1987, the court of appeals issued two orders. In the first, the court, sitting en banc, vacated its prior order setting the case for rehearing en banc and reinstated the portions of the opinion and judgment it had earlier vacated (86-1380 Supp. Br. App. SA-3 to SA-4). In the second, the panel vacated its earlier order denying the petitions for rehearing, granted the petitions, and reversed a portion of its opinion and judgment of January 6, 1987, concerning FERC's

The court concluded that "[t]he combined force of [Sections 201, 205 and 206, 16 U.S.C. 824, 824d, 824e] leads inexorably to the conclusion that, under the circumstances presented in the instant case, FERC had jurisdiction to modify the Grand Gulf allocation set forth in the UPSA" (Pet. App. 33a). "When, as here, generation capacity has been built and planned on a profoundly integrated basis, the Commission properly may examine its allocation as a cost component affecting wholesale rates" (*ibid.*). The court stressed that "[u]nreasonable disparities in the shares borne by affiliates of the total costs of the system's generating capacity plainly 'affect' the wholesale rates at which the operating companies exchange energy, and therefore require remedial action by the Commission pursuant to section 206" (*id.* at 35a). Finally, the court rejected petitioners' claims that FERC has unlawfully exercised jurisdiction over a generating facility, unlawfully compelled the purchase of generating capacity, impermissibly intruded on state jurisdiction, and taken action inconsistent with the Public Utility Holding Company Act (*id.* at 39a-57a).

ARGUMENT

Petitioners contend that the Commission lacked jurisdiction under the Federal Power Act to determine the just and reasonable allocation of Grand Gulf 1 capacity and costs among the four operating companies of the MSU system. The court of appeals' rejection of that claim

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allocation (*id.* at SA-5 to SA-6). In accordance with Judge Bork's partial dissent to the original panel opinion (Pet. App. 94a-96a), the remand is for FERC's "reconsideration of the decision to equalize the capacity costs of all nuclear plants, and for an explanation of the criteria used to determine what constitutes 'undue discrimination' and of why [FERC's] ultimate decision is not unduly discriminatory" (86-1380 Supp. Br. App. SA-6).

was plainly correct and is consistent with all pertinent decisions of this Court and other courts of appeals. Further review is not warranted.[8]

1. Section 206(a) of the Federal Power Act, 16 U.S.C 824e(a) (emphasis added), provides that whenever the Commission finds that any "contract *affect[ing]* [any] rate, charge, or classification [demanded, observed or collected by any public utility for any sale subject to the jurisdiction of the Commission] is unjust, unreasonable, [or] unduly discriminatory," the Commission shall "determine the just and reasonable * * * contract to be thereafter observed and in force, and shall fix the same by order." The Commission's jurisdiction to order a specific allocation of Grand Gulf 1 capacity and costs is squarely based on that specific directive: the contract provisions in question "affect" the four operating companies' "charges" to each other, as well as to public customers, in interstate wholesale transactions.

The four operating companies and MSE are all "public utilities." Each of them both produces and sells electric power at wholesale in interstate commerce: the four operating companies share the system's "capacity" and make "equalization payments" designed to align each company's share of the cost of total system capacity with its share of the demand for the system's energy (see Pet. App. 10a-12a); in addition, the four operating companies sell energy to each other, with the buyer always assumed to buy the lowest cost energy available in the pool after the

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[8] The court of appeals remanded to the Commission for further proceedings (see note 7, *supra*). The interlocutory posture of this case may itself justify denial of certiorari. However, because of the relationship between this case and *Mississippi Power & Light Co.* v. *State of Mississippi*, No. 86-1970, which is currently pending before the Court on the merits (see note 21, *infra*), we explain more fully why the decision below is correct and why the case does not present any issue that warrants this Court's consideration.

needs of the producer of that energy have been served (see *id.* at 11a & n.7); in addition, each of the four operating companies sells energy at wholesale to public customers (*id.* at 378a).

As the court of appeals said, although the provisions of the UPSA that allocate the capacity and costs of Grand Gulf "do not fix wholesale rates, their terms do directly and significantly *affect* the wholesale rates at which the operating companies exchange energy, due to the highly integrated nature of the MSU system" (Pet. App. 37a (emphasis in original)). The assignment of a specified amount of Grand Gulf 1 capacity to a particular operating company obviously affects both its obligation to pay (or right to receive) capacity "equalization payments" from time to time, and its need to buy (or ability to sell) excess power from (or to) other members of the system; in view of the pricing of pool exchanges under the System Agreement, the allocation of Grand Gulf 1 capacity also affects the prices at which such transactions occur.[9] In sum, the provisions the Commission reviewed here are an inseparable part of a set of interrelated agreements that set terms for interstate wholesale transactions between components of the MSU system, and they are exactly what Congress evidently intended to reach by the "contract affect[ing]" clause of Section 206(a).

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[9] The amount of Grand Gulf capacity allocated to an operating company affects the terms on which system power from Grand Gulf is available to that company. For instance, under the UPSA and 1982 System Agreement as originally filed with the Commission, AP&L, although not obliged to pay for any share of Grand Gulf capacity, would have been able to purchase electric energy from Grand Gulf through the system power pool at extremely low prices: under the 1982 System Agreement, prices for power pool transactions reflect variable costs (which for Grand Gulf are very low) and not fixed costs (which for Grand Gulf are very high). The cost of Grand Gulf power to the other operating companies, which were all allocated a percentage of Grand Gulf capacity, would, of course, have been much greater.

Petitioners contend (86-1380 Pet. 10 n.8; 87-469 Pet. 18-19) that the court of appeals' theory would extend the Commission's jurisdiction to labor contracts, construction contracts, and in general any contract that affects a utility's costs and therefore its rates. They are wrong for two reasons. First, the court of appeals affirmed the Commission's jurisdiction over these provisions *not* because they affect the wholesale rates the companies charge in sales to customers, but because they affect the meaning and operation of agreements governing transactions between the operating companies themselves: these provisions "affect rates" not merely in the sense that they tend to cause rates to be higher or lower, but by altering the practical operation of other agreements between the same companies that govern inter-company transactions that concededly *are* subject to FERC's jurisdiction. As the court of appeals said (Pet. App. 37a (emphasis deleted and added)), "the allocation of Grand Gulf capacity and costs * * * significantly affects the wholesale rates at which the operating companies exchange energy [with each other] due to the *combined effect* of the UPSA and the 1982 System Agreement."[10] Second, even as respects the effects on rates charged by a utility to wholesale customers, there is an obvious difference between a contract that merely sets a price to be charged to a utility by a third-party supplier and a contract that allocates a commonly-incurred cost between two utilities. FERC believes that it would have jurisdiction to reform the latter (if unjust) in connec-

[10] See Pet. App. 111a (footnote omitted) ("[W]e emphasize that the UPSA cannot be viewed in isolation. It is an agreement which 'supplements or supersedes' the coordination arrangements among the MSU utilities, and * * * is a contract 'affecting' rates under the 1982 System Agreement.").

tion with its review of wholesale rates for the two utilities, whether or not the two utilities are otherwise related.[11]

The breadth of FERC's jurisdiction over contracts "affecting" rates and charges was recently reaffirmed by this Court in *Nantahala Power & Light Co.* v. *Thornburg*, No. 85-568 (June 17, 1986). That case involved contracts between two affiliated utilities allocating a limited supply of low-cost power. Commenting on the binding effect of these contracts (as FERC-filed agreements) for state rate-making purposes, and on the Commission's power to modify the entitlements provided for, the Court said that while the terms of the agreements "do not purport explicitly to set a sales price for power, FERC's decision on how Nantahala may treat these agreements in determining its wholesale rates obviously does *affect* Nantahala's costs directly, and thus Nantahala's wholesale rates" (slip op. 17 (emphasis added)). As the court of appeals said (Pet. App. 38a), this decision provides a "clear and timely message that FERC's jurisdiction under such circumstances is unquestionable."[12] The same rationale has been accepted by every court of appeals to address the issue (see *Appalachian Power Co.* v. *Public Service Comm'n*, 812 F.2d 898 (4th Cir. 1987); *Minnesota* v. *FERC*, 734 F.2d 1286, 1287-1289 (8th Cir. 1984)).

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[11] See Pet. App. 342a-343a. Contrary to the assumption of petitioner Reynolds Metals (87-469 Pet. 17 n.17), the Commission's jurisdiction here does not depend on whether the Commission has a long-standing practice—which it does—of "rolling-in" jointly incurred costs to avoid unduly discriminatory rates.

[12] Neither of petitioners' objections to following *Nantahala* here has merit. First, it is true (see 86-1380 Pet. 19) that in *Nantahala* the Commission had merely set certain wholesale rates and had not altered the agreements themselves. But it was assumed in *Nantahala* that FERC could have altered the agreements, and indeed the case would have been one step easier had it done so: one *problem* in *Nantahala* was that the State was being compelled to honor, in setting Nantahala's retail rates, a reallocation that was not embodied in FERC-altered agreements but only in FERC's determinations for pur-

2. Petitioners claim (86-1380 Pet. 8-10; 86-1424 Pet. 5-7; 87-469 Pet. 21-23) that Section 201(b)(1), which limits the Commission's jurisdiction "over facilities used for the generation of electric energy" (16 U.S.C. 824(b)(1)), deprives the Commission of jurisdiction to reallocate the capacity of Grand Gulf. There are two dispositive answers. First, Section 201(b)(1) provides that "[t]he Commission * * * shall not have jurisdiction, *except as specifically provided* [elsewhere in the Act], over facilities used for the generation of electric energy or over facilities used in local distribution * * *" (16 U.S.C. 824(b)(1) (emphasis added)). Since the provisions in question here are, as explained above, contractual provisions affecting rates and charges for transactions within the Commission's jurisdiction, Section 206 "specifically provided" the Commission with jurisdiction to issue the reallocation order challenged in this case.

Second, the assertion of jurisdiction over contract terms affecting interstate wholesale transactions in the power produced by a particular generating facility simply is not the same as the assertion of jurisdiction over the "generating facility," within the meaning of Section 201(b)(1). That section plainly means to refer to such matters as the size, type, location, and operation of the facility, none of which FERC asserted jurisdiction over. See

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poses of a parallel proceeding setting Nantahala's wholesale rates; the Court solved that problem by noting that the Commission's order in the wholesale case was "for purposes of this case, essentially the same as reformation of the agreement itself" (slip op. 18).

Second, petitioner Reynolds Metals' reliance (87-469 Pet. 21 n.21) on the Commission's own distinction of *Nantahala* is misplaced. The Commission's remarks, which were made prior to this Court's decision in *Nantahala*, were expressly confined to factual distinctions that are relevant only to a legal issue (piercing the corporate veil) not presented by the petitions. See Pet. App. 124a; cf. *id.* at 169a (citing *Nantahala* as authority for the Commission's jurisdiction here).

Pacific Gas & Electric Co. v. *State Energy Resources Conservation & Development Comm'n*, 461 U.S. 190, 205-206 (1983). Although the Commission's order may affect some matters relating to generation, that, as the court of appeals said (Pet. App. 40a), is simply "the byproduct of a legitimate exercise of FERC's power to regulate wholesale rates" and not regulation of the facility itself.[13]

Nor, contrary to petitioners' claim (86-1380 Pet. 9; 86-1424 Pet. 5, 6; 87-469 Pet. 22-23), does this Court's decision in *Connecticut Light & Power Co.* v. *FPC*, 324 U.S. 515 (1945), suggest otherwise. In *Connecticut Light & Power*, the Court ruled that the Commission had no jurisdiction over the accounting practices of a utility whose facilities were used solely for "local distribution" of out-of-state energy because Section 201(b)(1) exempts "facilities used in local distribution" from the Commission's jurisdiction "except as specifically provided" elsewhere in the Act (16 U.S.C. 824(b)(1)). The reason the Court gave (324 U.S. at 531) was that allowing FERC to assert jurisdiction solely because of the carriage of some out-of-state energy "would nullify the exemption and transfer as a practical matter to Federal jurisdiction the regulation of many local companies that we think Congress intended to leave in state control." The present case, by contrast, involves a fundamentally interstate arrange-

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[13] Contrary to petitioner Reynolds Metals' claim (87-469 Pet. 18-19), the court of appeals' decision is not inconsistent with *FPC* v. *Conway Corp.*, 426 U.S. 271 (1976). In that case, this Court held that FERC should have considered certain matters concededly not within the Commission's jurisdiction in determining whether wholesale rates within the Commission's jurisdiction met applicable federal standards. The issue in this case is whether the allocation of Grand Gulf capacity *is* a matter within the Commission's jurisdiction, an issue on which *Conway* has no bearing.

ment that only FERC can regulate, and there is no danger of swallowing the "generating facilities" exemption, which serves an entirely different purpose.[14] Section 201(a) reveals Congress's understanding that there would be "Federal regulation of matters relating to generation to the extent provided in this subchapter and subchapter III" (16 U.S.C. 824(a)). And, as the court of appeals said, "[t]he Conference Report on the FPA instructs that the * * * phrase[] [in Section 201] ["except as specifically provided" elsewhere] w[as] 'added to remove any doubt as to the Commission's jurisdiction over facilities used for the generation * * * of electric energy to the extent provided in other sections' " (Pet. App. 40a (quoting H.R. Rep. 1903, 74th Cong., 1st Sess. 74 (1935)).

3. Petitioners claim (86-1380 Pet. 19-20; 86-1424 Pet. 6-7; 87-469 Pet. 15-16, 26-27) that FERC exceeded its authority by "forcing" AP&L to purchase Grand Gulf capacity. But AP&L is not entitled to be treated as if it were a stranger to the system. AP&L participated in the complex set of intra-system arrangements that allocate

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[14] The "local distribution" and "generating facilities" exceptions also differ in a material respect. As this Court stressed in *Connecticut Light & Power*, 324 U.S. at 524, FERC already exercises jurisdiction over wholesale rates before the electricity reaches the local distribution facility and therefore "[w]hat [the utility] does or fails to do is only after the incidence of federal regulation and can in no way frustrate it." But denial of FERC jurisdiction to regulate interstate wholesale transactions merely because they are described in terms of the output of a particular generating facility would have quite different effects, substantially frustrating important policies of the Act. Indeed, petitioners' view would permit companies engaging in interstate commerce to avoid federal regulation altogether by forming a generation-only subsidiary to engage in the wholesale sales to them. The court of appeals correctly rejected this illogical reading of the congressional design.

the costs and output from all of the system's generating capacity, and AP&L participated in the system decision to build Grand Gulf 1. Indeed, under the original plan, AP&L would have been responsible for 17.1% of Grand Gulf costs (see Pet. App. 398a) and, as FERC found (*id.* at 170a), AP&L still remains financially obligated to creditors for that amount in the event that the other operating companies fail to meet their obligations. FERC specifically rejected AP&L's claim that Grand Gulf "was planned only for the other operating companies" and FERC instead found that "AP&L has been continuously involved in the system decisions regarding Grand Gulf and MSE" (*id.* at 169a-170a; see *id.* at 397a-398a, 427a-428a). The Commission and the court of appeals concluded (*id.* at 43a-44a (footnote omitted) (quoting *id.* at 169a)) correctly that " 'the issue here is not whether a company should be forced to purchase or sell power, but rather is the appropriate allocation of costs among integrated companies owned by the same parent.' "[15]

As the court of appeals said (Pet. App. 44a), "[a] consistent line of judicial precedent" supports the Commission's assertion of jurisdiction in these circumstances. This Court's decision in *Pennsylvania Water & Power Co.* v. *FPC*, 343 U.S. 414 (1952), is most directly on point. There, the Court upheld the Commission's authority to require two unaffiliated utilities to continue their long-standing integrated activities, holding that integration was a "practice" affecting wholesale rates, and that the Commission could, therefore, require the utilities to "continue to *buy*, sell, and transmit power in the same coordinated manner

[15] Contrary to petitioner Reynolds Metals' apparent assumption (87-469 Pet. 16), AP&L was *not* a nonparty to the allocation; it was a party (to both the 1982 System Agreement and the UPSA) that received an allocation of 0%. The Commission's jurisdiction is just as clear as it would be if AP&L had originally been allocated some positive percentage that the Commission found to be unduly low.

in which [they] have been functioning * * *" (343 U.S. at 421 (emphasis added)).[16] Of course, the basis for Commission jurisdiction is even stronger in this case, because here FERC is regulating the interstate activities of affiliated members of a public utility holding company established (and given permission under the Public Utility Holding Company Act) to operate on a regional, integrated basis (see Pet. App. 46a).

Finally, petitioner Reynolds Metals' related assertion (87-469 Pet. 15) that the Commission lacks jurisdiction because Section 201(b) extends only to wholesale *sales*, not *purchases*, also fails. Section 201(b) is not so narrowly drawn and the Commission frequently approves provisions for a seller's wholesale rates that, in effect, limit the options of a purchaser.[17] Petitioners' reliance (87-469 Pet. 15) on this Court's decision in *Nantahala* for the contrary view is misplaced. The Court's arguendo assumption in *Nantahala*, slip op. 19—that "a particular *quantity* of power procured by a utility from a particular source could be deemed unreasonably excessive [by the state commission in setting retail rates] if lower-cost power is available elsewhere, even though the higher-cost power actually purchased is obtained at a FERC-approved, and therefore reasonable, *price*"—does not bear on this case at all. This is not a case of the kind there envisioned, where a utility

[16] Petitioners' attempt to distinguish *Pennsylvania Water & Power* is unpersuasive. Contrary to petitioners' claim (86-1424 Pet. 6-7; 87-469 Pet. 26-27), the Court's decision in that case did not turn on the narrow circumstance that the Commission was simply enforcing a preexisting contractual arrangement or merely requiring compliance with an outstanding Commission order. As described by the court of appeals (Pet. App. 45a n.77), the Court relied, more broadly, on the Commission's authority under Section 206. See 343 U.S. at 422-423.

[17] See, *e.g.*, *Kentucky Utilities Co.* v. *FERC*, 766 F.2d 239, 240-241 (6th Cir. 1985) (cancellation notice periods); cf. *Wisconsin Gas. Co.* v. *FERC*, 770 F.2d 1144, 1150 (D.C. Cir. 1985), cert. denied, 476 U.S. 1114 (1986) (minimum commodity bills) (FERC implementation of similar provision of Natural Gas Act).

purchases power from an affiliate at a FERC-approved *price* while "lower-cost power is available *elsewhere*" (*ibid.* (emphasis added)). Rather, this is a case like *Nantahala* itself, where all of the relevant sources of power, some of which are more expensive than others, are within the utility system and the sole question—one that only FERC can fairly resolve—is how the benefits and burdens of those sources should be shared among affiliated companies doing business in different states. In these circumstances, FERC must determine both the price and the quantity, as it has done in its allocation of Grand Gulf capacity.[18]

4. Petitioners' final claims that the court of appeals' decision will create an undesirable "regulatory gap" (86-1380 Pet. 10-15), will preclude an "entirely workable" scheme of state regulation (87-469 Pet. 27-28), and is contrary to the Public Utility Holding Company Act of 1935, 15 U.S.C. 79 *et seq.* (86-1380 Pet. 21-22; 87-469 Pet. 25 n.27), also warrant no further review.

First, no "regulatory gap" is created by the court of appeals' decision. Contrary to petitioner Arkansas Public Service Commission's assertion (86-1380 Pet. 13-15), FERC had the power to consider a claim—had one been made—that Grand Gulf 1 was an imprudent investment whose costs should be borne in whole or part by MSU stockholders rather than by the operating companies' ratepayers, and that MSE should therefore not be permitted to charge the operating companies 100% of the

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[18] Petitioners likewise err in claiming (86-1380 Pet. 6; 87-469 Pet. 21) that FERC's allocation has forced AP&L to share the benefits of its relatively inexpensive coal and nuclear generation capacity with the other three operating companies. As the court of appeals found (Pet. App. 53a n.93), this argument is "fallacious" because "[t]he reallocation of Grand Gulf simply adjusts AP&L's share of MSU's generation capacity costs—costs incurred jointly by the system." See also *id.* at 75a.

costs. But none of the parties, including those from Arkansas, made that argument to FERC.[19]

It is petitioners' crabbed view of the Commission's jurisdiction that would threaten to create a regulatory gap, in which no authority, state or federal, would have power to regulate important aspects of interstate arrangements for the wholesale sale of power. As this Court observed in *Arkansas Electric Cooperative Corp.* v. *Arkansas Public Service Comm'n*, 461 U.S. 375, 378-379 (1983), Congress adopted Part II of the Federal Power Act to provide federal authority to fill the regulatory gap created by the holding in *Public Utilities Comm'n* v. *Attleboro Steam & Electric Co.*, 273 U.S. 83 (1927), that states had no authority to regulate interstate wholesale electric rates. Without attempting to explore precisely the limits of state authority (in the absence of federal jurisdiction) over the present complex arrangements, it is at least highly likely that the states could not, either effectively or constitutionally, regulate the allocation of costs among the four utilities operating in four states of the MSU system. Indeed, each of the affected jurisdictions has sought to deflect the financial liability for the joint Grand Gulf enterprise onto the citizens of its neighboring states (see 87-469 Pet. 28 & n.33). As explained by the court of appeals (Pet. App. 51a-52a (footnote omitted) (quoting *id.* at 312a)), this is the sort of situation for which Congress concluded that FERC would be " 'in the best position to reach the most equitable result and to act in the public interest,

[19] FERC found (Pet. App. 183a-195a), moreover, that Grand Gulf 1 was part of a reasonable system plan to diversify the fuel base by developing nuclear power to meet anticipated growth in demand. FERC also explicitly affirmed and adopted (*id.* at 190a-191a, 216a) the findings and conclusions of its administrative law judge who determined that MSU's decisions both to begin and to complete construction of Grand Gulf 1 were prudent (see *id.* at 426a).

rather than to be controlled by the necessarily parochial concerns of the States.' "[20]

For this reason, petitioners' suggestion that FERC's assertion of jurisdiction is inconsistent with the Public Utility Holding Company Act of 1935 is also without merit. To be sure, that law sought to eliminate or simplify holding company systems to make the component utilities more amenable to state regulation. But it also specifically authorized the Securities and Exchange Commission to allow a holding company system to continue to exist upon a finding that a "single integrated public-utility system" can best serve a particular geographical region (see 15 U.S.C. 79k(b)(1), 79b(a)(29)). Congress placed such systems under comprehensive federal control because their activities "extending over many States are not susceptible of effective control by any State" (15 U.S.C. 79a(a)). The MSU system operates within that framework, and petitioners' claim that the court of appeals' decision is somehow inconsistent with the Public Utility Holding Company Act is wholly mistaken. See *Northern States Power Co.* v. *Minnesota Public Utilities Comm'n*, 344 N.W.2d. 374, 382 n.17 (Minn.), cert. denied, 467 U.S. 1256 (1984).[21]

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[20] Petitioners are mistaken in arguing (86-1380 Pet. 14; 87-469 Pet. 15 n.14, 21 n.21) that prior Commission decisions endorse the principle of state review of prudence in these circumstances. The Commission has carefully qualified that principle in cases, such as this one, involving affiliates. See *Kentucky Power Co.*, 38 F.E.R.C. ¶ 61,243, at 61,822-61,824 (1987), petition for review pending, No. 87-3643 (6th Cir.).

[21] In a related case, *Mississippi Power & Light Co.* v. *State of Mississippi*, No. 86-1970, the Court recently postponed consideration of jurisdiction to the hearing of the case on the merits. We do not, however, share petitioners' view (86-1380 Supp. Br. 3-4; 87-469 Pet. 28-29) that the Court should for that reason grant review in this case and either decide this case before deciding *Mississippi Power & Light*, or decide the two cases "in tandem." The issues presented in the two cases are entirely distinct, and the decision below in the present case is

CONCLUSION

The petitions for a writ of certiorari should be denied.

Respectfully submitted.

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in keeping with all relevant precedent and plainly correct. FERC's order in the present case is indeed a premise of the dispute in *Mississippi Power & Light*, but unwarranted prolongation of the meritless challenge to FERC's jurisdiction here will only complicate resolution of that dispute.

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